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Ratepayer Advocate
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March 9, 1998

Secretary
Federal Communications Commission
1919 M Street NW
Washington, D.C. 20554

Re: In the Matter of Petition of LCI Telecom Corp. for Declaratory rulings, CC Docket No. 98-5.

Dear Secretary:

The Division of the Ratepayer Advocate (Ratepayer Advocate) hereby submits its comments as an interested party in the above referenced proceeding. An original and 13 copies are enclosed. Please mark all copies as filed and return one copy in the self-addressed stamped envelope. Please add us to the service list for this proceedings.

The State of New Jersey
Division of the Ratepayer Advocate

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 98-5
Petition of LCI Telecom Corp.	)	
For Declaratory Rulings	)	

COMMENTS TO LCI'S PETITION

INTRODUCTION

The Division of the Ratepayer Advocate ("Ratepayer Advocate"), State of New Jersey, is a separate independent state agency established under N.J.S.A. 13:1-D-1 for the expressed purpose of protecting the consumers' interest in all matters affecting public utilities. The Ratepayer Advocate represents the interests of all classes of ratepayers and is authorized to appear on behalf of ratepayers in various matters that are before the New Jersey's Board of Public Utilities ("BPU"), a State commission as defined in the Communications Act of 1934, as amended. This includes matters associated with the implementation of the Telecommunications Act of 1996 ("Act" or "1996 Act") 47 U.S.C. § 151 *et. seq.* The Ratepayer Advocate strongly supports the Act and its intended benefits to all ratepaying consumers. The petition filed by LCI Telecom Corp. ("LCI") directly affects ratepayers and rights established under the Act and the Ratepayer Advocate's mandate is within the zone of interest to be protected. The Ratepayer Advocate has previously participated in other Federal Communications Commissions' ("FCC") proceedings such as interconnection and Universal Service. The Ratepayer Advocate also will participate in any proceedings conducted by the BPU in connection with Section 271 of the Act. In view of the foregoing, the Ratepayer Advocate is an interested party for purposes of submitting comments in this matter.

EXECUTIVE SUMMARY

The Ratepayer Advocate believes that the petition of LCI should be denied and dismissed. LCI's petition is contrary to the Act. LCI submits that its proposal would hasten the Regional Bell Operating Companies (RBOCs) entry into interlata services. However, LCI's proposal as offered limits and/or expands the checklist established by Section 271(c)(2)(B) of the Act in violation of the Section 271(d)(4) of the Act. The FCC is precluded from taking such action by Section 271(d)(4) of the Act. In addition, the grant of the LCI's petition would foreclose facilities based competition in the local exchange market -- one of the goals that the Act was intended to achieve -- and perpetuate the local exchange monopoly of each RBOC.

BACKGROUND

LCI filed its petition entitled "Fast Track Proposal" with the FCC on January 22, 1998. The FCC subsequently issued a public notice requesting that any interested party could file comments by February 25, 1998 and reply comments by March 27, 1998. On February 20, 1998, the FCC issued an order revising the periods for submission of comments and reply comments to March 23, 1998 and April 22, 1998 respectively. LCI asserts that it filed this Fast Track Proposal to spur and foster the promise for competition that the 1996 Act offered. LCI states that meaningful competition has not materialized because there are three primary barriers that preclude competition:

1. The absence of nondiscriminatory operations support systems (OSS).
2. No practical and efficient unbundled network elements (UNEs).
3. Pricing that discriminates in favor of RBOC's own retail operations.

According to LCI, these barriers preclude the RBOCs from otherwise meeting the requirement of Section 271 of the Act which establishes a 14 point checklist that must be met before a RBOC could enter the long distance market place in the states they operate in as a local exchange carrier. LCI submits that these barriers exist because a common thread is present. That common thread is that RBOCs have a conflict of interest between both their roles as network supplier and service provider; that is, RBOCs have no incentive to sell use of their local exchange facilities (generally referred to as Facilities Based Network) to competitors on a wholesale basis when doing so will result in the RBOCs' retail side of the business losing customers and revenue.

LCI's answer to remedy the conflict of interest is that the FCC should adopt the LCI's Fast Track Proposal. Under the Fast Track Proposal, a RBOC would be granted faster entry into the long-distance market if the RBOC agrees to create a corporate structure in which the RBOC (referred to as the "HoldCo") would separate its operating business into two entities, a retail service company ("ServeCo") and a wholesale company to manage the network ("NetCo"). According to LCI, such separation would create a rebuttable presumption that the requirements of Section 271 and the 14 point checklist have been met. LCI postulates that if seven minimum elements are required and implemented, the conflicts of interest would be eliminated and entry into the long-distance market would be hastened. The seven elements are:

1. NetCo and ServeCo would not share facilities, function, services, employees or brand names;
2. NetCo would not engage in any retail marketing, but would continue to service its existing customer base on a transitional basis until those customers are won by ServeCo or other retail competitors;
3. NetCo would deal with ServeCo only on an equal (not "separate but equal") basis with all other new entrants -- such as LCI -- who use NetCo's network to provide local phone service;
4. Substantial public ownership of ServeCo (approximately 40% or more);
5. Independent directors on the ServeCo board, including representatives of the non-HoldCo shareholders;
6. Compensation for ServeCo management based only on ServeCo performance, not the performance of HoldCo or NetCo; and

7. As a key transitional matter, ServeCo would not provide stand-alone long-distance service to a NetCo customer until customers can be switched among competing providers of local service as easily as they are switched among long-distance companies today. At that point, a state commission could also decide to require balloting and allocation of NetCo's remaining customer base.

DISCUSSION

THE FAST TRACK PROPOSAL IS IN CONFLICT WITH THE TELECOMMUNICATIONS ACT OF 1996 AND WOULD REQUIRE SUBSTANTIAL REVISIONS OF THE ACT IN ORDER FOR THE FCC TO BE ABLE TO IMPLEMENT LCI'S PROPOSALS.

Under the Act of 1996, Congress wanted to offer the RBOCs the carrot of participation in the long-distance market as an inducement for LECs to open the local exchange market to competition through the offering of access and interconnection to other carriers. Compliance by the RBOC with the access and interconnection requirements of the Act were to be measured by application of the 14 point check-list of Section 271 of the Act. The FCC has the sole right to determine whether the 14 point checklist has been met by an applicant subject to the requirement that the FCC consults with the Attorney General of the United States and with State commissions in accordance with Section 271(d)(2). The FCC has the final approval or rejection authority. In approving or rejecting an application, Section 271(d)(4) of the Act restricts the FCC from limiting or extending the terms used in the competitive checklist. This section on its face would therefore expressly preclude the FCC from being able to adopt LCI's Fast Track Proposal, even if the FCC were otherwise so inclined. Furthermore, there are other parts of LCI's Fast Track Proposal that are at odds with the purposes of the Act that likewise require its denial and dismissal.

Congress correctly envisioned that if access and interconnection were provided to other carriers, there would be the prospect of meaningful competition in the local exchange market which would permit long-distance entry by the RBOCs, and they passed the Act to further meaningful competition. Access and interconnection were to be fostered by mandating interconnection in accordance with Sections 251 and 252 of the Act. Principally, this required the local exchange company to provide interconnection through UNEs and through resale of services based upon wholesale prices so that a facilities based competitor as defined under Section 271(c)(1)(A) of the Act materialize. Section 271(c)(1)(A) provides in pertinent part;

> For the purpose of this subparagraph, such telephone exchange service may be offered by such competing providers either exclusively over their own telephone exchange service facilities or predominately over their telephone exchange services facilities in combination with the resale of the telecommunications services of another carrier.

If one or more facilities based competitors exist, then the FCC can accept applications and review them for compliance with the 14 point checklist. As discussed below, if LCI's proposal was granted, there would never be competition in the local facilities based network arena. This is contrary to and inconsistent with the Act.

The RBOCs' NetCo would in effect be granted a monopoly for network services; the very thing the Act was intended to prevent. LCI's proposal ensures that a RBOC would never face wireline network competition because all carriers would have to purchase the network from NetCo and NetCo has no competitors. It is highly unlikely that a competitor would develop due to the high cost of building a competing network. Even if a potential competitor did arise, it is less than certain how State commissions would regulate the NetCo and the new entrant. As a monopoly, NetCo should probably be regulated on the classic rate of return approach. However, NetCo's network has been paid for and subsidizes its current rates. A new entrant would have the initial cost of building a network and have to amortize those costs over some period. Under rate of return theory, the rates of the new entrant have to exceed the NetCo rates because the new entrant's cost base -- upon which rate of return -- is determined will be higher then the NetCo's cost basis for its network. If rate cap regulation was involved, even more complex questions are presented. In the final analysis, facilities based competition will not develop in the local exchange market if the Fast Track Proposal is adopted.

More importantly, the proclaimed benefit, elimination of conflicts of interest, would not occur but would continue on a different level. Although LCI submits that its identified barriers to entry create irreconcilable conflicts of interest for the RBOCs that preclude or inhibit the opening of RBOCs' networks on non-discriminatory terms, LCI's Fast Track Proposal does not cure the conflicts but merely creates new conflicts without achieving facilities based competition. The Fast Track Proposal as proposed is directly at odds with one of the basic underpinning of the Act, i.e., to foster facilities based competition in the local exchange market. Structural separation does not eliminate or preclude conflicts of interest.

For example, NetCo could provide network access to all carriers but never enhance or improve the network. As a result the NetCo's network would not be updated for new technology or services. At the same time, ServeCo -- NetCo's sister company -- could take over all independent research and development and implement through hardware and software changes new or innovative improvements to enhance the basic service obtained from NetCo. As a consequence, ServeCo would be in a position to maintain its market share and offer additional service features superior to its retail competitors. Of course, ServeCo's competitors would be stuck with the unenhanced basic service and would not learn of additional service features until ServeCo offered the additional service to the public. Such a scenario could be highly anticompetitive.

Correspondingly, NetCo would be in a position to goldplate its network with costly and expensive changes or enhancements that no one wants and which do not improve service or features. Under rate of return regulation, NetCo's cost would be in its rate base and subject to rate of return calculation. NetCo as a practical matter has a cost contract that results in higher dollars of return and profit for increasing its costs. Clearly, the potential conflicts of interest under LCI's proposal are not eliminated but they only resurface in other ways. A rate cap regulatory environment further complicates the issues since NetCo cannot be forced to adopt rate caps. The probable outcome is more regulation not less regulation. There are too many subtle ways to subsidize and maintain market share that can only be remedied by a comprehensive regulatory program. The Fast Track Proposal is not a comprehensive regulatory program. Congress envisioned something more when it balanced the various concerns by mandating compliance with Sections 251 and 252 of the Act, including pricing, non-discrimination, and other provisions.

LCI points to the deregulation of the electric industry as support that its Fast Track Proposal will work. However, there are important differences which makes its comparison inappropriate and irrelevant. In the electric utility area, there are multiple generators of electricity at the lowest level of the market chain. The deregulation of electric utility is founded on the premise on that the consumer should be able to buy electric power from that the least cost generator and have that power delivered through the transmission and distribution lines operated by the local utility. Electric power is a fungible product. It is irrelevant whether it is produced in California or New York. If the generator has a more efficient plant and equipment and can produce power for less, there is a nationwide market for that fungible product. If competition exists at the generating side then competition can exist at the end user side. Telephone service is not a fungible product on a nationwide basis. It depends on individual and separate exchange networks serving specific geographic locations. In the field of electric utility, competition exists at the product generation level, but in the telephone arena, competition does not exist in the local exchange market. LCI's Fast Track Proposal, instead of eliminating the problem, exacerbates the problem by ensuring that local exchange competition will never occur.

LCI emphasizes that its approach will eliminate or reduce the delays encountered to date in implementation of the Act. However, LCI's Fact Track Proposal is inconsistent with the Act since it would contravene Section 272(d)(4) by improperly expanding and at the same time limiting rights afforded under the Act. To accomplish this, the FCC would need to have Congress amend the statute. In light of the contentious nature of pending legal proceedings under the Act to date and the several proposals voiced by Senators and Congressman for revising the Act, one should not anticipate that amendments to the Act would be any less contentious. A new level of delay and uncertainness would be added to the process precluding the competition envisioned by the 1996 Act. An amendment of the statute is not likely anytime soon while the processes implementing the congressional mandate of the Act are well underway. Though the development of competition is not moving as quickly as some would like, it is working consistent with the statutory parameters of the Act. Within the next year, more parts of the picture will be in place. If the rules of the game are to change, such change should be initiated by Congress and not the FCC, especially when Congress has precluded the FCC from expanding or limiting the Section 271 process. Changing course in mid stream will lead to further delays, not increased competition.

Assuming one could overcome the legal restrictions set forth in Section 271(d)(4) of the Act, adoption of LCI's Fast Track Proposal will not result in:

Faster advent of local competition, especially for residential Consumers,
Simplification of Section 271 compliance,
Reduced regulation,
Promotion of Universal Service,
Enhanced maintenance of network quality and reliability, or
Other proffered benefits.

Although the Fact Track Proposal was intended to bring competition to the market place, the plan set forth by LCI, which rests upon structural corporate changes that separate the network function from the retail functions to eliminate the incentive to discriminate and to level the playing field for retail competition, is fundamentally flawed. The limited role of State commissions in the opening of the interlata market to RBOCs will be greatly expanded without any additional assurances that such state involvement will hasten the sought after facilities based competition.

CONCLUSION

For the reasons set forth above, the Ratepayer Advocate respectfully asks that LCI's petition be denied and dismissed.

Sincerely,

The State of New Jersey
Division of the Ratepayer Advocate

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